

pricing flexibility and a sharing mechanism, both of which could be used to recover reasonable costs. GTEC's deregulation concern is premature. For example, yellow page directory services and inside wire services developed at ratepayers' expense and subsequently deregulated are currently reflected in the NRF sharing calculation. Any concern regarding recovery of PBOP costs associated with future deregulated services should be addressed in the proceeding that considers deregulation of those services.

The utilities under NRF should establish a regulatory asset in their regulatory financial statements to reflect yearly differences, if any, between their PBOP costs being expensed and their tax-deductible contributions. Similar treatment should be provided for in their external financial statements.

## **2. Rate Base Consideration**

The utilities were divided as to whether the regulatory asset should be given rate base treatment. However, DRA recommended that regulatory assets should not receive rate base treatment and that if we determined it imprudent to fund PBOP costs beyond some level, ratepayers should not be burdened with the responsibility to pay a return on funding PBOP in excess of the prescribed level. DRA took this position because the utilities would not be funding the regulatory asset. According to DRA, its position to exclude the PBOP regulatory asset from rate base was also the position of Edison, PG&E, and SoCal Gas.

Three utilities recommended that rate base treatment be given to the PBOP regulatory asset. The utilities that recommended such treatment were GTEC, Pacific Bell, and SDG&E. However, SDG&E clarified that rate base treatment was dependent on whether its regulatory asset was being funded.

DRA recommended that the utilities be ordered to not include any PBOP regulatory assets in rate base without explicit authorization to do so. There was very little testimony on this issue. However, because the regulatory asset will not impact the

utilities' cash flow until the utilities are able to make additional tax-deductible contributions, we concur with DRA and will adopt DRA's recommendation that PBOP regulatory assets not be included as part of rate base.

## **XII. Legislative Impacts**

In opening this investigation we were generally aware that Congress was considering a bill which, if passed, would allow the transfer or use of excess pension assets for PBOP. We immediately recognized that this could be an effective way of funding PBOP because it would not involve additional charges to current ratepayers and it would not result in any loss of tax revenue to the United States Treasury. Therefore, Congressional legislation was identified as an issue and respondent utilities were requested to report the effects of any proposed Congressional legislation related to PBOP in the second phase of this investigation.

Except for SoCal Gas, the respondent utilities were not aware of any Congressional legislation that could potentially affect PBOP. Although SoCal Gas testified that it was aware of several bills that have been introduced which could potentially affect PBOP, it was not able to identify any specific bills or to provide a current status of such bills at the evidentiary hearing. SoCal Gas did testify that because there was no real consensus formed to support any of the bills that any possibility of such bills being passed was pure speculation.

Of the three interested parties participating in this phase of the investigation, only DRA addressed potential legislative impacts. DRA's testimony corroborated the respondents' general consensus that there was no pending legislation. However, DRA did recommend a list of areas that should be explored in considering the effects of proposed Congressional legislation.

DRA's checklist may be helpful in analyzing the effect of future legislation. However, such a checklist is not useful in this proceeding because no party has identified any pending legislation that the checklist could be applied to. DRA apparently agrees with this conclusion because its witness recommended that this proceeding not remain open to consider potential future legislation. Absent any testimony to the contrary, the legislative impacts issue need not be addressed as it has no present impact in this investigation.

### **XIII. Safeguard Mechanism**

An integral part of our PBOP investigation is to address safeguards needed to protect ratepayers' interest upon the adoption of accrual accounting for PBOP. Three safeguard concerns were identified in this phase of the investigation. Two of the concerns are identical to the safeguard concerns addressed in the first phase of this investigation. They are that PBOP funded amounts will be used for only PBOP and the need for necessary monitoring procedures to track plan activities and performance. The third concern (not previously addressed) is whether full recovery of accrued PBOP will reduce incentives for the utilities to aggressively negotiate PBOP with employee unions.

DRA acknowledged that regulators, such as the Commission, are prohibited under the NLRA and by court decisions from "prescribing" outcomes for collective bargaining. However, DRA emphasized that the utilities are given no regulatory assurance of rate recovery for negotiated agreements between the utilities and the unions for unfair or unreasonable arrangements. Such regulatory review of negotiated agreements has traditionally taken place in general rate proceedings. However, DRA is concerned that there is no safeguard to prevent the utilities' management from conducting labor negotiations between test years in order to

maximize excess funding. Therefore, DRA concluded that adoption of the Statement for ratemaking purposes may risk unreasonable funding, resulting in both rate shock and rate volatility.

On the other side of this issue, the utilities asserted that full funding of PBOP will not, in any way, compromise good faith negotiations with unions regarding the level of retirement benefits provided to employees.

PG&E's Richard Weingart explained that although the NLRA's good faith bargaining rule does not have a provision which protects ratepayers' interest, the utilities maintain a strong economic motivation to negotiate labor contracts which reduce the overall cost of the utilities' operations. This economic motivation is enhanced by expanded competition within the industry requiring the utilities to keep their rates within a competitive level.

Weingart further explained that it is not appropriate to isolate a single issue, such as PBOP, in the broad context of the collective bargaining process because collective bargaining encompasses a multitude of issues which require the giving and taking of concessions. From the utilities' perspective, a primary interest in the collective bargaining process is controlling the costs of operations. To assess that controlling interest one can not assess the reasonableness of PBOP as a single issue without regard to other provisions agreed upon in the negotiation of a labor agreement.

Irrespective of assessing PBOP as a single negotiation issue, several of the utilities substantiated that they have reduced and are continuing to reduce PBOP costs through the collective bargaining process. For example, PG&E implemented several PBOP plan changes as a result of its 1991 contract negotiations which resulted in a PBOP cost reduction of approximately \$4 million. Pacific Bell's Dennis Evans also

testified of PBOP cost containment measures which were implemented by Pacific Bell in the past few years.

There is nothing in the record to demonstrate that the utilities will have any less incentive to aggressively negotiate PBOP benefits in good faith if they are authorized full recovery of accrued PBOP costs. On the contrary, the evidence substantiates that the utilities have every incentive to continue negotiating cost containment to their respective PBOP plans.

DRA's and the utilities' testimony on our first two safeguard concerns mirror their respective testimony in the first phase of this investigation. Because we have already found that sufficient FASB, IRS, ERISA, and NLRA reporting, disclosure, and fiduciary requirements are in place to ensure that funds placed in a PBOP plan will be tracked and will be used only for PBOP, there is no need to require redundant safeguards at this time. To require supplemental safeguard procedures will only increase the cost of providing PBOP.

However, this is not meant to preclude in any fashion CACD or DRA from requesting and obtaining additional data from the utilities regarding their PBOP activities. Consistent with our Phase I position, we will take the most conservative approach as it relates to PBOP funding and require that the utilities establish trusts for the receipt, investment, administration, and disposition of any PBOP funds which we may authorize the utilities to recover in rates. As a condition of the recovery process of PBOP costs being authorized in this order, the utilities should continue to be required to make their trust agreements readily available to CACD and DRA upon their request.

#### **XIV. Z Factor Treatment**

In the first phase of this investigation GTEC and Pacific Bell requested Z factor recovery treatment for their PBOP

contributions. However, because of an incomplete record, their request was deferred for consideration to this phase of the investigation. Prior to considering Z factor recovery treatment, it is necessary to review how the Z factor was established and the required criteria to recover cost.

**A. Z Factor Criteria**

D.89-10-031, 22 CPUC 2d 43 (1989), established a NRF for GTEC and Pacific Bell. This NRF centered around a price cap indexing mechanism that was designed to provide protection to both ratepayers and shareholders from risks that the indexing method may over- or underestimate revenue changes needed to keep the utilities financially healthy. At the same time, the price cap indexing mechanism placed on GTEC's and Pacific Bell's management more responsibility to control their expenses and to assume more risks in exchange for simplified regulation and an opportunity to earn higher rates of return.

The Z factor was established as the component of the price cap mechanism to protect both the ratepayers and shareholders against exogenous events which affect utility costs but are not reflected in an economy-wide GNPPI.

The NRF decision concluded that only exogenous factors which are not reflected in the economy-wide inflation factor and which are clearly beyond the utility's control should be reflected in the Z factor in the price cap index (22 CPUC 2d at 228). That decision also recognized that the range of exogenous factors which could affect utility costs to an extent warranting explicit rate adjustments through the Z factor cannot be foreseen completely. However, the following factors were accepted as a starting point:

1. Changes in federal and state tax laws to the extent they affect the utilities disproportionately.
2. Mandated jurisdictional separations.

3. Changes to intraLATA toll pooling arrangements or accounting procedures adopted by this Commission.
4. Changes in regulatory amortizations.
5. The reflection of tax benefits resulting from premature retirements of high coupon bonds.

GTEC and Pacific Bell contend they should be able to recover pre-funded PBOP contributions and future PBOP costs they will incur due to the adoption of the Statement as a Z factor.

**B. Recovery of Pre-Funded PBOP Contributions**

GTEC pre-funded \$27.1 million in a fully tax-deductible bargained VEBA in December of 1991 and anticipated pre-funding an additional \$25.2 million in 1992 in order to mitigate the impact on GTEC's ratepayers of implementing the Statement if the accounting change is adopted for ratemaking purposes.

Pacific Bell pre-funded PBOP contributions of \$117 in 1989 and \$91 million in 1990. However, it discontinued making further pre-funded contributions in 1991 and 1992 because of the uncertainty that it would recover in rates its pre-funded contributions in a timely manner and because of the many demands for its capital resources. Upon assurance that PBOP contributions would be recovered in rates on a timely basis, Pacific Bell would be willing to continue pre-funding in 1992. If the Commission denies recovery of its pre-funded contributions for 1989 and 1990, then Pacific Bell's TBO would need to be re-calculated to reflect a higher obligation.

DRA opposed both GTEC's and Pacific Bell's request for Z factor recovery of their pre-funded contributions for two reasons. First, DRA believed that such recovery would constitute retroactive ratemaking. Second, DRA does not believe pre-funded contributions satisfy the Z factor criteria established in the NRF decision.

Both GTEC and Pacific Bell exercised good intentions in pre-funding their PBOP costs to minimize the ratepayers' impact associated with the Statement by utilizing tax-deductible trusts which accumulated tax-free earnings. Nevertheless to authorize Z factor recovery, we must first conclude that pre-funding meets the criteria established in the NRF decision.

There is no dispute that the Statement will have a material impact. However, DRA does not believe that GTEC's and Pacific Bell's pre-funding activities meet the criterion that pre-funding is clearly beyond the utility's control.

Pre-funding was authorized in the first phase of this investigation. However, it was authorized on a permissive basis. No utility was required to make pre-funded contributions. Although this permissive pre-funding was effective August 1, 1991, Pacific Bell actually began pre-funding in December 1989.<sup>26</sup> Clearly, Pacific Bell's pre-funding of 1989 contributions was not beyond its control, especially since its contributions were made almost two years prior to Commission authorization and a full year prior to the FASB's adoption of the Statement. Similarly, Pacific Bell's 1990 contributions were made almost eight months prior to Commission authorization.

Pacific Bell's decision to discontinue pre-funding and to not pre-fund in 1991 and 1992 further substantiated that pre-funding was not only permissive but was well within the utilities' control. Pacific Bell's proposal to continue pre-funding in 1992 if assurance is given that rate recovery will be provided on a timely basis continues to substantiate that pre-funding is in the control of the utilities.

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<sup>26</sup> We also note that Pacific Bell's 1989 pre-funded contribution took place within two months after the NRF decision was issued.



Neither GTEC nor Pacific Bell has met its burden of proof to demonstrate that pre-funded contributions were clearly beyond their control. Absent such a finding we must deny GTEC and Pacific Bell authority to recover pre-funded PBOP via the Z factor. Because pre-funded contributions have not met the Z factor criteria, the retroactive ratemaking issue raised by DRA is moot and need not be addressed.

**C. Recovery of Funded PBOP Contributions**

GTEC and Pacific Bell believe that Z factor recovery is applicable for accrued PBOP costs because these costs satisfy the criteria established in the NRF decision. Once again, the criteria consist of exogenous factors which are clearly beyond the control of the utilities and which are not reflected in the economy-wide GNPPI.

The utilities explained that the control factor will be met if we adopt the Statement because they will have no choice but to implement accrued PBOP. DRA agreed with the utilities that the adoption of the Statement is clearly beyond the utilities' control and that such action would be an exogenous factor.<sup>27</sup> However, DRA argued that the utilities do not satisfy the control criterion because the utilities control PBOP costs. For example, the utilities will have the ability to control the amount of funded accrued liability, select the appropriate funding mechanism, and reduce or increase their PBOP expenses.

No party disputed DRA's contention that the utilities have the ability to control the day-to-day management of PBOP

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27 DRA went on to provide conflicting testimony on whether such an exogenous factor exists because of the economic nature of PBOP costs. Its direct testimony stated that an exogenous factor does not exist because there are no major changes to the economic cost of providing PBOP, Exhibit 75 page 69. However, DRA's witness subsequently testified that the cost change does exist from an economic standpoint, RT 1105 Line 13.

costs. However, the same is true of most other factors that may qualify for Z factor treatment. For example, changes in federal and state tax laws, identified in the NRF decision as a Z factor adjustment, are beyond the control of the utilities. At the same time, the utilities will continue to control the actual payment of taxes and the level of taxes resulting from the tax change.

Ordering Paragraph 26 of the NRF decision stated in part that only exogenous factors which are clearly beyond the utility's control should be reflected in the Z factor. There is no mention of costs in the ordering paragraph. The word "factors" identified in the ordering paragraph represents exogenous activities beyond the utilities' control, such as accounting and tax law changes.

To the extent that the utilities incur costs to comply with these exogenous factors, such costs satisfy the Z factor control criterion. Therefore, costs associated with the change from cash to accrual accounting for PBOP not recovered through the GNPPI should be recovered through a Z factor adjustment.

Both GTEC and Pacific Bell conducted detailed studies on the impact that the Statement would have on the GNPPI to assure that double recovery would not take place. Although the utilities used consistent economic theory in their studies, they did use a different behavior assumption related to whether firms already considered accrued PBOP costs in their hiring and output decisions.

Pacific Bell's study assumed that competitive firms were already making their hiring and output decisions on the basis of accrued PBOP while GTEC took the conservative approach and assumed the opposite of Pacific Bell. Their results were similar. GTEC concluded that the GNPPI would recover 0.73% of the additional cost while Pacific Bell concluded that the GNPPI would recover 0.12%.

DRA concluded that some degree of rate recovery already exists in the GNPPI because health care, dental care, and life insurance components are components of the GNPPI. It was apparent that GTEC and Pacific Bell did not disagree with DRA because they

quantified the impact, although not material, in their respective studies. Pacific Bell further clarified that the Z factor adjustment is necessary to reflect accrual accounting while the GNPPI reflects the change in inflation for PBOP gross national output price increases.

In this instance we have the benefit of two different economic studies which demonstrate that the GNPPI will not be impacted to any significant degree. Although economic studies, such as the ones used by GTEC and Pacific Bell, are objective, the results are dependent on the subjective inputs. From these subjective inputs the parties advance arguments in support of their respective analyses and in criticism of the input assumptions used by other parties. In the final analysis, it is the application of judgment, not the precision of these economic studies, which is the key to determining the extent of impact.

Our analysis of the evidence shows that the GNPPI will be impacted minimally, as demonstrated by the utilities' economic studies. This analysis of the evidence also leads us to conclude that the recovery of the accrual required by adopting the Statement with modification through the Z factor will not provide the utilities with any measurable double recovery through the GNPPI adjustment. Based on our judgment, the NRF utilities should be authorized to use the Z factor adjustment to recover accrual impacts from adopting the Statement as modified by this order.

In relation to Pacific Bell's economic study, GTEC's study was very conservative. In fact, GTEC attempted to determine whether adoption of the Statement would impact other components of the GNPPI. Based on its additional analysis, GTEC concluded that some of the costs associated with the change in GNPPI may influence wage rates in the national economy. If the wage rate in the national economy is reduced in relative terms due to the impact of the Statement, an additional 14.38% of the PBOP costs may be recovered by GTEC in the GNPPI due to a reduction in the wages that

GTEC pays to its employees relative to what it would have paid in the absence of the Statement.

Although GTEC's study shows that it could receive additional recovery benefits through the wage component of the GNPPI, there is no evidence in the record to substantiate or to sway our judgment that NRF utilities will, in fact, receive any additional recovery benefits. Because there is a possibility that the NRF utilities may receive ancillary benefits to the detriment of ratepayers, we do not want to foreclose future consideration of GTEC's speculative result. It would be best to consider this issue after the Statement has been implemented and after a period of time has lapsed so that we may draw upon historical data. Therefore, as part of their October 1993 price cap filing, GTEC and Pacific Bell should include studies to demonstrate whether the wage component of the GNPPI has been affected by adoption of the Statement and recommendations on how the impacts, if any, should be reflected in rates.

**Findings of Fact**

1. This investigation was opened to assess the ratemaking treatment of PBOP and to consider the establishment of consistent general policies and procedures for PBOP.

2. The funding of PBOP with tax-deductible trusts is in the ratepayers' best interest.

3. The utilities have been given permissive authority to fund and to recover their PBOP costs prior to the Statement's effective date.

4. The Statement requires all entities to replace the prevalent practice of recording PBOP benefits on the cash basis of accounting with the accrual basis of accounting.

5. The Statement will become applicable to California regulated utilities effective January 1, 1993.

6. GTEC's, Pacific Bell's, and SDG&E's average residential customer's bill will increase \$0.38, \$0.75, and \$0.19 per month if the Statement is adopted without modification.

7. SoCal Gas was granted authority to fund PBOP and to implement rates to recover PBOP costs in its Test Year 1990 GRC.

8. It is not feasible for the utilities that are pre-funding PBOP to true-up their PBOP costs in this investigation.

9. Standard and Poor's and Moody's already factor in the effect of PBOP liabilities.

10. The additional PBOP reporting required by the Statement would be helpful for the rating agencies to fine-tune their assessments and could even reveal a significantly smaller burden than previously assumed by the rating agencies.

11. The higher, or more favorable, the rating given to the utilities' debt by rating agencies, the lower the costs, or interest rate, to service debt.

12. A correlation exists between debt and common equity risk.

13. There is no basis to conclude that the Statement would have any measurable impact on the companies' ability to access capital markets.

14. Inter-generational inequity will not be resolved by adopting the Statement without modification.

15. Adoption of the Statement would place the recovery of PBOP on a more consistent basis with the recovery of pension and nuclear decommissioning costs.

16. PBOP, pensions, and nuclear decommissioning funding must currently recognize the expense of liabilities that will not come due for a considerable period of time.

17. The absence of a specific code requirement for the recovery of PBOP costs is not a basis to treat PBOP costs differently from the recovery of decommissioning cost.

18. Code sections that mandated a funded accrual basis of cost recovery for nuclear decommissioning were not added to the

code until 5 years after we authorized energy utilities to implement an accrual basis of accounting for decommissioning costs.

19. The Nuclear Decommissioning Act did not come into existence until 3 years after utilities were authorized to fund their decommissioning cost on an accrual basis of accounting.

20. PBOP are currently being paid in a manner similar to pension benefits.

21. The funding of pensions in advance of the utility's payment of benefits is a proper cost of service.

22. The USOA Rewrite decision was applicable to only regulated telephone utilities and did not automatically adopt future GAAP changes for regulatory purpose.

23. The funding of PBOP on an accrual basis can provide an economic advantage over the cash basis method.

24. Rate shock represents an increase of 1% or more of total operating revenue.

25. Procedures can be implemented to mitigate any rate shock.

26. The basic cost of service policy dictates that the utilities should have the opportunity to recover in rates reasonable operating expenses, including PBOP costs, taxes, and a fair return on invested capital.

27. The controlling element in fixing rates is what it costs the utility to perform service.

28. The utilities have already taken steps to contain and to reduce PBOP costs.

29. Shareholder and employee funding of PBOP is not a viable funding alternative at this time.

30. Utilities need union approval to use excess pension assets for PBOP.

31. IRC § 420 provides for the limited transfer of excess pension assets to a § 401(h) account for only the years 1991 through 1995 and only if the pension plan is fully funded.

32. A majority of the utilities do not have surplus pension funds.

33. Surplus pension assets generally result from volatile changes in the investment markets which cannot be predicted with any accuracy.

34. Surplus pension assets are not a viable funding alternative for PBOP costs.

35. Cost of service is an indispensable factor in setting fair and reasonable rates for regulated service.

36. Employees do not qualify for PBOP unless they specifically provide utility service for a minimum period of time.

37. Similar to the receipt of pension benefits, employees are not entitled to receive PBOP until after they retire from utility service.

38. The longer that employees work, the less expensive the cost of PBOP paid for by ratepayers.

39. Approximately one-third of the TBO represent PBOP applicable to current retired employees.

40. Similar to pension benefits, PBOP actuarial reports would be performed on a periodic basis to reflect changes in actuarial assumptions including plan benefits, inflationary factors, and mortality rates.

41. The Statement's method of accounting for PBOP on the accrual basis of accounting meets the cost of service criterion.

42. The cash basis of PBOP recovery fails to incorporate the cost of service principle.

43. The accrual basis of revenue recovery meets the assurance criterion and provides a degree of certainty that sufficient funds will be available to pay the utilities' PBOP costs.

44. Adoption of the Statement would give the utilities flexibility to assess PBOP on an ongoing basis.

45. Employees are not earning an incremental increase in PBOP as the employees age.

46. The Statement's benefits/years-of-service method provides for a disproportionate allocation of benefits cost over the employees' working life.

47. It is reasonable to ratably flow through the cost of the employees' PBOP over the employees' entire working life.

48. The Statement's 20-year amortization method of TBO benefits will substantially mitigate inter-generational inequity.

49. Ratepayers would be required to pay an additional \$670,000 for every \$1 million that the utilities contribute to taxable PBOP funded plans.

50. The funding of PBOP with tax-deductible contributions enhances a balance of interest between shareholders and ratepayers.

51. The FASB allows utilities to reflect a regulatory asset in their external financial statements with the assurance that such costs will be recovered through rates in the future.

52. The SEC has not taken a policy position on what criteria should be used to determine whether a regulatory asset should be allowed.

53. Reasonable PBOP costs are defined to be those PBOP costs applicable to regulated services that meet the Statement criteria as modified by this order and are invested in tax-deductible plans administered by an independent trust, that are necessary to meet funding requirements based on fair actuarial assumptions, contributions, and investments, and that are not used to enhance pension benefits.

54. The regulatory asset will not impact the utilities' cash flow until the utilities are able to make additional tax-deductible contributions.

55. The utilities have every incentive to continue negotiating cost containment to their respective PBOP plans.

56. There are sufficient FASB, IRS, ERISA, and NLRA reporting, disclosure, and fiduciary requirements in place to



ensure that funds placed in a PBOP plan will be tracked and will be used for only PBOP.

57. A Z factor was established as a component of the price cap mechanism for NRF utilities to protect both ratepayers and shareholders against exogenous events.

58. Only exogenous factors which are not reflected in the GNPPI and which are clearly beyond the utility's control can be reflected as a Z factor adjustment.

59. The first phase of this investigation authorized pre-funded PBOP contributions on a permissive basis.

60. Pacific Bell began pre-funding PBOP in December 1989, almost 2 years prior to Commission authorization and a full year prior to the FASB's adoption of the Statement.

61. Pacific Bell chose not to pre-fund PBOP in 1991 and 1992.

62. Pacific Bell will continue to pre-fund PBOP in 1992 if assurance is given that rate recovery will be provided on a timely basis.

63. The adoption of the Statement is clearly beyond the control of the utilities.

64. To the extent that the utilities incur and manage cost to comply with exogenous factors, such cost satisfies the Z factor control criterion.

65. The Z factor adjustment is necessary to reflect accrual accounting while the GNPPI reflects the changes in inflation for PBOP gross national output price increases.

66. Economic studies demonstrate that the GNPPI will not be impacted to any significant degree by adoption of the Statement.

67. It is possible that the NRF utilities may receive ancillary benefits to the detriment of ratepayers through the GNPPI wage factor with the adoption of the Statement.

#### Conclusions of Law

1. Affected utilities should true-up their PBOP costs as part of their next GRC filing or price cap filing.

2. The recovery of PBOP costs for regulatory accounting ratemaking purposes should be based on consistent cost of service policy and cost recovery mechanisms.

3. The Statement as modified by this order should be adopted for regulatory accounting and ratemaking purposes.

4. The Statement's benefits/years-of-service approach should not be adopted for regulatory accounting and ratemaking purposes.

5. The utilities should use the employees' total service life attribution method to distribute the cost of employees' PBOP benefits for both the TBO and ongoing PBOP cost.

6. The utilities should amortize the TBO over 20 years.

7. The utilities under the traditional ratemaking and the telecommunications utilities under the NRF process should recover their PBOP costs in rates to the extent that they are able to make contributions to tax-deductible plans.

8. Commission policy should not be governed by whether or not utilities can record a regulatory asset under Statement No. 71.

9. Regulatory accounting and ratemaking should not be governed by IRS, ERISA, or SEC requirements.

10. The utilities should establish a regulatory asset.

11. The recovery of tax-deductible contributions in any given year should be limited to a maximum increase of 1% of the utilities' prior year's total operating revenue.

12. Recovery of the regulatory asset should begin during the year when tax-deductible limits exceed PBOP costs and continue until the regulatory asset has reached a zero balance.

13. Regulatory assurance language should be included in rate orders which address rate recovery of PBOP costs.

14. Any concern regarding recovery of PBOP costs associated with future deregulated services should be addressed in the proceeding that considers deregulation of those services.

15. The PBOP regulatory asset should not be a component of rate base subject to a return on investment.

16. The utilities should establish trusts for the receipt, investment, administration, and disposition of PBOP for any PBOP funds which we may authorize the utilities to recover in rates. Earnings of such trust may be taxable to the trust or to the employees.

17. The utilities under the NRF should not be allowed to recover their pre-funded PBOP contributions through the Z factor adjustment because they have not demonstrated that funding PBOP prior to adoption of the Statement with modification was beyond their control.

18. Effective January 1, 1993 with the adoption of the Statement as modified by this order, NRF utilities should be allowed to recover reasonable costs associated with the change from cash to accrual accounting through the Z factor adjustment.

19. NRF utilities should include as part of their October 1993 price cap filing a study to demonstrate whether the wage component of the GNPPI has been affected by the Statement and should make recommendations on how such impact, if any, should be reflected in rates.

#### O R D E R

##### **IT IS ORDERED that:**

1. The Financial Accounting Standards Board Statement of Accounting Standards No. 106 (Statement), Employers' accounting for post-retirement benefits other than pensions (PBOP), shall be adopted with the following modifications, as discussed in this order, for regulatory accounting and ratemaking purposes and shall be effective January 1, 1993, the effective date of the Statement.

- a. The employees' total service life attribution method shall be used to distribute the cost of employees' PBOP for both the transition benefit obligation (TBO) and ongoing PBOP costs.

- b. The Statement's benefits/years-of-service approach shall not be used for regulatory accounting and ratemaking purposes.
- c. The TBO shall be amortized over a 20-year time period beginning January 1, 1993.

2. Regulated utilities under traditional cost-of-service ratemaking and the new regulatory framework (NRF) shall be authorized to recover their PBOP costs associated with the adoption of the Statement to the extent that the utilities:

- a. Establish and use independent trusts for the receipt, investment, administration, and disposition of PBOP.
- b. Make tax-deductible contributions which do not need to be grossed up by a net-to-gross multiplier. Earnings to the trust may be tax-free or taxable to the trust or employees.
- c. Use PBOP trust funds for only PBOP.
- d. Incur PBOP costs that are necessary to meet funding requirements based on fair actuarial assumptions, contributions, and investments.
- e. Do not use PBOP to enhance pension benefits.
- f. Limit yearly recovery of PBOP costs to a maximum increase of 1% of the utilities prior year's total operating revenue.

3. The utilities shall establish and maintain a regulatory asset pursuant to Financial Accounting Standards Board's Statement No. 71 and as discussed in this order. The recovery of such regulatory asset to be recovered in future rates shall begin during the year when tax-deductible limits exceed PBOP costs and shall continue until the regulatory asset has reached a zero balance.

4. The regulatory asset required by this order shall not be considered a rate base component subject to a return on investment.

5. GTE California Incorporated (GTEC) and Pacific Bell shall not be authorized to recover their pre-funded PBOP costs through the Z factor adjustment provided for under the new regulatory framework.

6. Effective January 1, 1993 GTEC and Pacific Bell shall be authorized to recover through a Z factor adjustment their PBOP costs associated with the change from cash to accrual accounting as provided for in this order.

7. GTEC and Pacific Bell shall include as part of their October 1993 price cap filing a study to demonstrate whether the wage component of the Gross National Product Price Index has been affected by PBOP and to recommend how such impact, if any, should be reflected in rates.

8. Those utilities that are tracking their pre-funded PBOP contributions in an interest-bearing memorandum account pursuant to Ordering Paragraph 5 of Decision 91-07-006 shall be authorized to continue inputting interest on such contributions up to January 1, 1993, the effective date of the Statement. Interest shall not continue to accrue after the effective date of the Statement.

9. Utilities operating in other jurisdictions with their California operations being 10% or less of their total utility operations shall be allowed to be exempted from the accrued PBOP requirements imposed by this order. However, for ratemaking purpose, such utilities shall be required to impute the effect of accrued PBOP, as explained in this order, as a part of future general rate filings. Such utilities shall also assume that their funding begins on January 1, 1993 and that earnings on their imputed PBOP contributions will be set at their authorized weighted cost of capital rate.

10. Pacific Gas and Electric Company's PBOP issue left open in Application (A.) 88-12-005 and Investigation (I.) 89-03-033 which was consolidated into this investigation has been resolved.

Accordingly, A.88-12-005 and I.89-03-033 are no longer consolidated with this investigation.

11. This decision disposes of the issues in our PBOP investigation. Accordingly, this proceeding is closed.

This order is effective 30 days from today.

Dated \_\_\_\_\_, at San Francisco, California.

## APPENDIX A

### List of Appearances

**Respondents:** John Barker, for California American Water Company; Beck, Young, French, & Ackerman, by Jeffrey F. Beck and Sheila B. Brutoco, Attorneys at Law, for Citizens Utilities Company of California; Kenneth K. Okel and Kathleen S. Blunt, Attorneys at Law, for GTE California Incorporated; Vicki L. Thompson and David R. Clark, Attorneys at Law, for San Diego Gas & Electric Company; William A. Ettinger, Attorney at Law, for AT&T Communications, Inc.; E. Garth Black, Attorney at Law, for Roseville Telephone Company; Orrick, Herrington & Sutcliffe, by Robert Gloistein, Attorney at Law, for Contel of California, Inc.; Robert B. Keeler and John R. Fallon, Attorneys at Law, for Southern California Gas Company; Richard S. Jarrett, for CP National; Robert M. Johnson, Attorney at Law, for Southwest Gas Corporation; Daniel J. McCarthy and Gregory L. Castle, Attorneys at Law, for Pacific Bell; Roger J. Peters, Kermit R. Kubitz, and Gary P. Encinas, Attorneys at Law, for Pacific Gas and Electric Company; Richard K. Durant, Carol B. Henningson, M. D. McDonald, and Frank A. McNulty, Attorneys at Law, for Southern California Edison Company; Robert A. Loehr, Attorney at Law, and Fred R. Meyer, for San Jose Water Company; and James D. Salo, Attorney at Law, for Sierra Pacific Power Company; Stoel, Rives, Boley, Jones & Grey, by Robert V. Sirvaitis and James C. Paine, Attorneys at Law, for Pacific Power & Light Company.

**Interested Parties:** Brown, Bridgman Retiree Health Care Group, by Stanley H. Clow and Fred D. Van Remortel; Nossaman, Guthner, Knox & Elliott, by Jose E. Guzman, Jr., Attorney at Law, for Westport Management Services, Inc.; Thomas Long and Michel Florio, Attorneys at Law, for Toward Utility Rate Normalization; and Norman J. Furuta, Attorney at Law, for the Department of Navy and Federal Executive Agencies.

**Division of Ratepayer Advocates:** James S. Rood and Rufus G. Thayer, Attorneys at Law, and Mark Loy.

(END OF APPENDIX A)

**APPENDIX B**

**List of Abbreviations and Acronyms**

AICPA Committee	- American Institute of Certified Public Accountants' Public Utilities Committee
ALJ	- Administrative Law Judge
ARA	- Attrition Rate Adjustment
CACD	- Commission Advisory and Compliance Division
Code	- Public Utilities Code
D.	- Decision
DRA	- Division of Ratepayer Advocates
Edison	- Southern California Edison Company
ERISA	- Employee Retirement Income Security Act
FASB	- Financial Accounting Standards Board
FCC	- Federal Communications Commission
GAAP	- Generally Accepted Accounting Principles
GNPPI	- Gross National Product Price Index
GRC	- General Rate Case
GTE	- GTE California Incorporated
I.	- Investigation
IRC	- Internal Revenue Code
IRS	- Internal Revenue Service
LEC	- Local Exchange Companies
Moody's	- Moody's Investigators Services, Inc.
NLRA	- National Labor Relations Act
NRF	- New Regulatory Framework
OII	- Order Instituting Investigation
PBOPs	- Post-Retirement Benefits Other Than Pensions
PG&E	- Pacific Gas and Electric Company
PU	- Public Utilities
Roseville	- Roseville Telephone Company
SDG&E	- San Diego Gas & Electric Company
SEC	- Securities and Exchange Commission
SFAS 106	- Statement of Financial Accounting Standards No. 106
SoCal Gas	- Southern California Gas Company
Southwest Gas	- Southwest Gas Corporation
Statement	- Statement of Financial Accounting Standards No. 106
TBO	- Transition Benefit Obligation
USOA	- Uniform System of Accounts
VEBA	- Voluntary Employee Benefit Association

**(END OF APPENDIX B)**